"Toronto Dominion Bank"

An Address by
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to the
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As your Chairman has indicated, the subject of my remarks today is one of paramount interest to me – banking and the Toronto Dominion Bank.

The Toronto Dominion is the fifth largest Canadian bank and you might expect that our prime objective would be to become the largest. This is not the case. Some of our competitors had a big head start on us. Rather, our ambition is to strengthen our reputation as the *best* Canadian bank. If we can achieve that, growth will take care of itself.

In comparing Toronto Dominion's size with the other major banks, one must keep in mind that all of them achieved their present status, in part, from a number of mergers or take-overs. In the case of Toronto Dominion, on the other hand, there has been only one.

A legal description of Toronto Dominion would be "A Canadian Chartered Bank", but as a description of its operations that term is somewhat superficial. Toronto Dominion is a savings bank, a commercial bank, a retail bank, a wholesale bank, a mortgage bank, a merchant bank and an international bank all rolled into one.

Canadian Needs Paramount

This combination of roles enables Toronto Dominion to assume major responsibilities in the domestic economy and we have recently been responding to the challenge of re-stimulating the Canadian economy since the Central bank began to relax its restraints early in 1970. Across a broad front, manufacturers, consumers, housebuilders and businessmen in general have been turning to us on an increasing scale to finance the spending required by an economy which is moving well into the recovery phase. This is as it should be, for, as a bank, our prime responsibility and our clear objective is to service the needs of Canadians. While I wish, later in this speech, to deal in some detail with lesser known aspects of our banking operations – for example, our international banking – I wish to emphasize at the outset that Toronto Dominion always places the needs of its domestic savers and borrowers in a paramount position.

I am sure you are all familiar with the monthly breakdown of the assets and liabilities of the Canadian banks which appears in the *Canada Gazette*. I have no intention of getting into a detailed discussion of these figures. You have

probably analyzed them in considerable depth. However, there are some important trends indicated by them to which I would like to direct your attention. These figures show that Toronto Dominion is growing faster than its major competitors. This is true of both Canadian and international business.

Increased Market Share

Toronto Dominion's share of the net Canadian deposits of all Canadian banks has risen from 10.9 per cent in January 1967 to 12.0 per cent at the end of July this year. The significance of using the year 1967 is that this was the first year of full disclosure and the New Bank Act.

In light of the competitiveness of the Canadian banking market, I think you will agree that this is a good performance. We believe *our* people *do* make the difference. This growth in market share reflects an aggressive marketing and branch development program which in the past five years has seen our Canadian branch network expand by116 to 790 offices. Our branch representation is greatest in Ontario so an increasing amount of attention is being given in our development plans to the establishment of new branches in other areas of Canada, particularly those communities where Toronto Dominion has not previously been represented.

In the foreign currency area, our record of growth is even better than in the domestic market. Toronto Dominion now has 13.7 per cent of the foreign currency assets held by the Canadian banking system, as against only 9.1 per cent in January, 1967.

Foreign Currency Deposits

From January, 1967 to July 31 this year, foreign currency deposits held by Toronto Dominion more than tripled to $1,712 millions. They now constitute 27.5 per cent of our total deposits.

In accordance with sound banking practice, foreign currency deposits are invested in four categories (1) deposits with other banks (2) securities (3) call loans and (4) commercial loans. Recently we have been especially active in making foreign currency commercial loans.

In January 1967, Toronto Dominion had only a modest volume of foreign currency commercial loans – $171 millions, equivalent to 7 per cent of

the foreign currency commercial loans of all Canadian banks. Our record of expansion in this area in the past 4½ years is impressive, such loans having more than tripled to $617 millions. Today we account for 12.4 per cent of the foreign commercial loans of all Canadian banks and expansion continues. Since October 31, 1970 we experienced an increase in the commercial loan area of 19.8 per cent.

The recent economic changes in the United States and the subsequent rapid adjustments in foreign exchange markets have not altered the outlook for growth. During the period since August 15 the Euro-dollar market remained active and has shown again it is mature and broad enough to withstand periods of uncertainty.

International Operations Profitable

You must keep in mind that our competitors in the international field are not only the Canadian banks but all international financial institutions, including the largest European and U.S. banks. To assist in obtaining this new loan volume primarily from governments and large multi-national corporations, we have been opening representative offices abroad. Previously, our only offices outside Canada were in the United States and the United Kingdom. Now, we have offices in Tokyo, Hong Kong, Djakarta and Mexico City with others planned. Not only do we have an agency in San Francisco, but our new subsidiary Toronto Dominion Bank of California recently opened for business in that city.

Is foreign business profitable? The answer is an emphatic "Yes". As was pointed out in our nine-months statement "improved results from our international operations were an important factor" in the increase in earnings which we were able to report.

Prior to 1968 many 3 to 5 year loans were made at fixed rates. Most of these have been retired and term loan rates are on a floating basis, geared to the roll over of the supporting deposit. The most popular method of quotation involves an appropriate margin, say 1% over the 6 months cost of Euro-dollar deposits to the bank. The loan may be for 5 years but the rate changes each 6 months during the period. Currency options of Deutsche marks and Swiss francs are often given but the important point is that the margin to the bank is fixed. This should mean that earnings on foreign

currency loans will be much more directly related to growth than has been the case in the past.

No Exchange Exposure

Also, because loans are funded by matching deposits, the percentage of loans to total deposits can rise. In the past, foreign currency loans of banks have averaged around 30% of foreign currency deposits, whereas a domestic ratio of 65% has not been unusual. We can foresee a time in the near future when the ratio of bank foreign currency loans, in Euro-dollars, to deposits, will rise to 50 or 60% and as loans are more profitable than the inter-bank deposits they replace on the asset side of the balance sheet, the return on capital should rise.

One last comment on our International business. We do not have an exchange exposure. Our foreign assets are funded from like currency deposits. In other words, the Canadian dollar deposits we collect in Canada are not used to fund foreign assets. This is a very important point as some people apparently feel we take funds from Canada to use in our International operations and this is not the case. Indeed, some of our foreign currency lending takes place in Canada and for Canadian projects.

I have followed with interest the amount of innovative analyses undertaken by financial analysts across the country with respect to bank stocks. I appreciate how difficult some of this work has been and would like to congratulate you on the results of your efforts. Perhaps I can make some comments with a view to opening the door a little wider with respect to an appraisal of some items on the asset side of a bank's balance sheet.

International Banking Affiliates

In recent years Toronto Dominion has invested substantial amounts in certain types of companies in Canada and abroad. These investments were made primarily to develop the Bank's capability in certain fields, one of these being the international banking area.

Toronto Dominion was the first Canadian bank to help establish a separate international banking organization. In 1964, we joined with three other leading world banks to form Midland and International Banks Limited (more commonly known as MAIBL) with headquarters in London, England.

MAIBL's capital is 10 million pounds sterling in which Toronto Dominion has a 26 per cent interest. Since its founding MAIBL's assets have grown to 491 million pounds sterling or $1.2 billion Canadian as at March 31, 1971. In addition, its earnings record has been excellent. Profits, after taxes in the year ended March, 1971, amounted to 1.4 million pounds sterling or $3.5 million Canadian. This is a 14% return on the original investment after tax and a 8% dividend was paid at year-end. Earnings currently are running well ahead of last year.

Over the past seven years MAIBL has made loans for substantial amounts to finance large scale development projects in all parts of the world.

Another international banking organization in which Toronto Dominion has a substantial interest – 30% – is the World Banking Corporation with headquarters in Nassau, Bahamas. Our major partner is The Bank of America. Assets of World Banking Corporation at more than $200 millions are eight times greater than when we acquired our interest five years ago.

Expansion in Asia

During the past 12 months Toronto Dominion has moved into Asia in a substantial way. In December last, in association with a group of South-East Asian businessmen, we participated in the formation of International Consolidated Investments Limited, Hong Kong. This company holds a major interest in two Hong Kong banks – the Overseas Trust Bank and the Hong Kong Industrial and Commercial Bank – and also has a strong association with the United Malayan Banking Corporation of Kuala Lumpur, Malaysia. Also included in its functions is the arranging of debt and equity financing for major projects in South-East Asia. Outstanding capital of International Consolidated Investments Limited is $HK 100 million ($16.75 million Canadian) and Toronto Dominion holds a 40 per cent interest.

Four months ago we strengthened our association with the United Malayan Banking Corporation by acquiring a 10 per cent direct interest. United Malayan has assets in excess of 700 million Malaysian dollars ($236 million Canadian) and has branches throughout Malaysia and Singapore as well as in Brunei and Bangkok.

From what I have said you will appreciate that considerable asset values have been built up behind

our banking investments. These, however, are not reflected on the asset side of our balance sheet since investments are carried at cost. They have real potential for growth in the future.

Real Estate Investments

A similar situation exists with respect to our investment in the Toronto-Dominion Centre. As you know, we have a 50% common stock interest in the Centre and this investment is also carried at cost. The approximate finished cost of this project was $145 millions, whereas its replacement value today would be close to $200 million. The earnings record to date indicates that TD Centre was, and is, an excellent investment. It has developed a positive cash flow and, as you know, we are going ahead with a third tower of 32 storeys.

In the first two towers, Toronto-Dominion Centre has two and a quarter million square feet of office space. With rental rates in the present prime space market approximating $10.00 per square foot and original leases made during the 1965-68 period averaging $7.25, together with the fact that 95% of the cost of the project has been financed for 25 years at an average rate of 6.08%, the potential for increased cash flow is available as the present leases mature. The average lease term in downtown office buildings in Toronto is close to 15 years. These are a few statistics which should assist you in realizing what a valuable asset we have in this prime North American location.

We are officially opening Toronto Dominion Bank Tower in Pacific Centre, Vancouver, tomorrow. We are a one-third partner in Pacific Centre. We are also 30% partners in Edmonton Centre, which will get underway next year. You may well ask why we are getting so involved in downtown real estate projects. There are several reasons. First, as experience with Toronto-Dominion Centre proves, they are a good investment. Secondly, they help the bank to develop a favourable image. Finally, the downtown area of any major city is a very important source of banking business and a branch located in a large building is in a strong competitive position. While on the subject of real estate, I might mention that the bank has a great many branches across the country sitting on valuable corners and the real value of these are not reflected in our real estate account. The Toronto Dominion Bank is one of Canada's largest real estate investors.

Venture Capital Banking

Earlier I remarked that "merchant banker" is one of the descriptions that fits Toronto Dominion. Some years ago the bank recognized the need for sources of capital to entrepreneurs and companies in their formative stages which could not provide the security commonly required by banks against loans and also were not sufficiently developed to seek public financing through investment houses. The T.D.'s response was to help organize and invest in venture capital companies. The bank has now over $3.5 million invested in venture capital type organizations. Besides the direct investment benefit that can accrue from these, the bank can and does gain from the exposure to companies that turn out to be major customers as they grow and prosper. Another benefit is the opportunity to participate in second stage financing, for example, convertible debentures and equity-linked loans.

One example would be our participation with UNAS Investments Ltd., and other investors in Lake Ontario Steel Company. After the successful proving at Whitby, Ontario, of Lasco's mini-mill concept for production of a small range of steel bar and rod products from scrap using electric arc melting, the group with local investors built a similar facility in Minneapolis, Minn. and now another multi-million dollar facility is under construction in the U.K. at Sheerness outside London. The bank's investment with those of the others in the group has been through a holding company, Co-Steel International Ltd. This is merchant banking in the true sense and is a meaningful way in which the bank can assist in the export of Canadian Technology.

Financial Packaging

In the bank we have people capable of handling the many special situations which arise in a world of increasing financial sophistication and specialization. Examples of this would be receivable financing in the needle-trade, term financing for new mines, construction loans on real estate projects bridging through to the mortgage financing, assisting and advising companies on acquisitions and mergers. In these areas, the bank, by having in-house expertise, is able to provide the funds in the correct form for the borrower and, as in other areas of our consumer economy, the product – money in this case – can often command a premium if it is packaged for maximum con-

venience to the consumer and combined with professional financial counselling.

We in the bank are responsible for identifying and appraising thoroughly new growth segments in the Canadian economy and positioning the bank so that it can capitalize on this expertise and participate in the segment's growth. An example of this would be our work over the last few years in the Cable T.V. industry.

As you know, we are now in the mortgage business in a big way, both directly and indirectly. Our mortgage operation is comprised of two portfolios – (1) mortgages we service and hold for our own account and (2) mortgages we process and service for other investors, institutions and individuals.

Mortgage Activity

At July 31 last the combined total under administration was $429 millions. Of this amount, $287 millions was for the bank's own account. During 1971 we expect to commit in excess of $130 millions in new funds for residential mortgages. This would indicate that in the near future we will have $500 millions of mortgages under administration.

Toronto Dominion mortgage approvals in the nine months ended July 31, 1971 totalled $101 millions, equivalent to 13.9 per cent of the approvals by all banks.

Another arm of our mortgage activity is Tordom Corporation, formed two years ago, in which Toronto Dominion has a direct stock interest of 50 per cent. Tordom issues paper with a term of up to five years and uses these funds to invest in top-grade N.H.A. and conventional mortgages. As at July 31, Tordom held a mortgage portfolio in excess of $55 millions.

About five years ago, due to the considerable increase in activity on the part of department stores, oil companies, travel and entertainment companies, and others, we found it necessary to assess the implications of our bank becoming involved in the all-purpose charge card business.

You will appreciate that the massive increase in charge card or credit card usage heralded the arrival of a new payment mechanism, and we decided to protect our bank's position at the core of the national payment structure and launch, in association with three other Canadian banks, the Chargex programme. You are all aware, of course,

that the bank charge card serves two purposes. First, it provides a method of payment to the cardholder and, secondly, a convenient form of open-ended credit covering relatively small amounts.

The Toronto Dominion Bank has invested a substantial sum in the development of this programme and you will not be surprised to learn that losses have been incurred in the start-up period. We have also been competing effectively with two other banks twice our size and we are in a position today where Toronto Dominion enjoys a much greater share of the public's bank charge card business than it does of the country's banking business as a whole.

What was a major innovation in Canadian financial affairs just three years ago has now become a household word, and as Chargex profitability emerges from the initial red figures, we confidently expect our bank's position to be excellent relative to its competitors.

Debenture Financing

Another change in Canadian banking resulting from the 1967 revision of the Bank Act is the manner in which banks can raise capital funds. Prior to that time Canadian banks were forced to increase their equity from time to time in order to maintain their capital ratios at acceptable levels. The need for additional capital resulted from the rapid growth of assets at a rate faster than the growth in retained earnings. A contributing factor was the relatively high dividend output. The high cost of raising such capital hindered the returns which the banks were able to achieve on their equity.

Some banks, including Toronto Dominion, have taken advantage of a less expensive way of raising additional capital – debenture financing. In fact, we were the first bank to do so. This, together with a somewhat lower percentage of earnings payout has enabled us to maintain our capital asset ratio at an adequate level. I am sure you are aware that our payroll ratio has decreased over the past four years.

As for the future, I think you can take it for granted that we will continue to issue debentures to raise additional capital. I can hear you asking the question, "Does this mean you do not intend to raise capital in the future through the issuance of rights to shareholders to subscribe for additional stock?" All I can say in answer to that is maybe

yes, maybe no. It is important that we keep our capital asset ratio at an acceptable level and certainly now the lowest cost way to raise additional capital is by the debenture route.

As financial analysts you watch our quarterly statements but they do not include the accumulated appropriation account except at year-end. During the past few years we have made substantial provisions to write down our corporate and municipal bond holdings to market value and these have been reflected in this account. Under required reporting procedures, Government of Canada and Provincial Securities are carried at amortized cost. However, with a much improved bond market in 1971 there should be some substantial recoveries in the Corporate and Municipal account at year-end. This will add to our capital base.

I am well aware that you attach more importance to balance of revenue after full income tax but before appropriation for losses than you do to balance of profits after appropriations and taxes and I must say I agree with you. As a matter of fact I think there are strong and sound arguments for changing our reporting procedure to more clearly highlight balance of revenue and we have the matter under study.

Earnings Above Average

Taking balance of revenue after adjustment for income taxes at an assumed rate of 50 per cent, you will find that Toronto Dominion's per share earnings have from 1967 to date been consistently above the average for the five major banks. Per share earnings on this basis have risen from $1.03 in 1967 to $1.85 in 1970. Based on the experience in the first nine months, I would say we can look for a balance of revenue after tax of approximately $2 a share for the full year.

I think you will agree that these are favourable results.

In conclusion let me turn for a moment to the outlook for 1972. We feel there will be a substantial growth in commercial loans and a moderation in the rate of increase in the money supply.

In light of the probable increase in loan income we are confidently expecting an even better year in 1972 than in 1971.

And now I would be pleased to answer any questions you may have.

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